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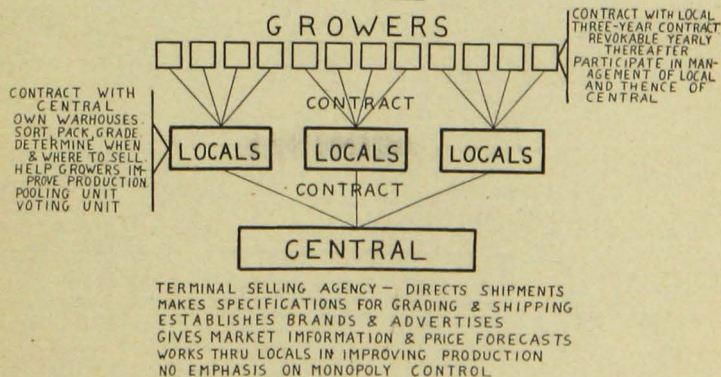
COOPERATIVE CENTRAL MARKETING ORGANIZATION¹

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SUMMARY

Any analysis of co-operative associations in the central markets soon reveals the fact that there are two important types so far as methods of operation, form of organization, and purposes are concerned. These are the so-called "federated" type and the "centralized," sometimes called "commodity," type. Altho different organizations within each type vary greatly, four important differences are

A GENERALIZED FEDERATED MARKETING ORGANIZATION



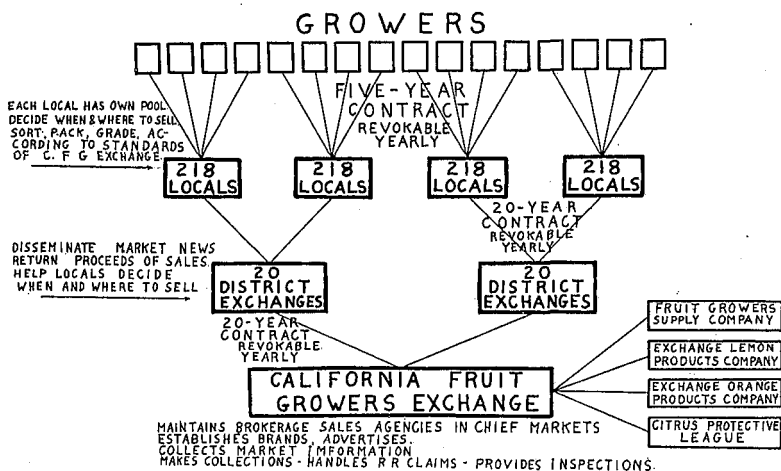
always present. Stated in terms of the centralized type of organization, these differences are as follows: (1) Abolition of the local co-operative unit as a pooling unit; (2) membership in the central organization or some mechanical subdivision of it, rather than in the

¹ From Agricultural Experiment Station Bulletin 211.

local unit; and membership contracts on the same basis; (3) complete control of the product—as to “when” to sell it and as to “where” to sell it, and how to grade and pack it; (4) control of all or a large part of the supply in order to be able to name a price and make it effective. This latter feature is likely to become less distinctive when the centralized plan is applied to grain, livestock, and other commodities produced over a wide territory.

No clear-cut classification can be made on this basis. It can generally be said, however, that as a federation takes on one or more of these features such as No. 1 or No. 3, it is verging toward the centralized type, and on the contrary, any centralized organization which has locals, which leaves the control of when and where to ship mostly with the local, or which in other respects does not have all of these four characteristics, is tending in the other direction. The Minnesota Co-operative Creameries Association, Incorporated, for example, is a federation, but is now taking on No. 1 and No. 3 to some extent. On the other hand, the Sun-Maid Raisin Growers, which meets all the tests of a centralized association, is organizing locals which are expected to play an important part in marketing California raisins.

ORGANIZATION OF CALIFORNIA FRUIT GROWERS EXCHANGE



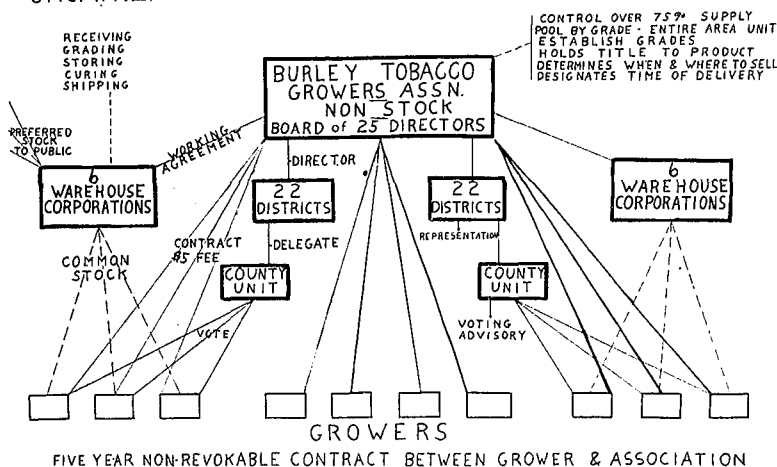
When these four differences were applied as a test to one hundred central market co-operatives located in thirty-three states, the organizations were found divided about equally between the centralized and the federated types. Centralized organizations predominate in the south and west, where the chief products are perishable, are poorly

standardized, and are marketed through decentralized marketing systems. Federations are more common in the North Central states, where local co-operation is best developed and where the principal products are staples, are better standardized, and are marketed through centralized marketing systems.

Milk producers' associations obviously do not fit into this classification and they are not included in the number of organizations summarized. They are really locals that coincide with the whole market area and that emphasize the control of a large part of the supply because the milk distributing business is in a relatively few hands.

Other characteristics, as the length and use of the membership contract, provision for damages for breach of contract, method of incorporation (stock vs. non-stock with subsidiary warehousing corporations), handling non-member business, combining the marketing of two or more products, selling methods, and the degree of integration, might also be noted. These differences, however, when applied as tests to the centralized and federated associations, do not prove to be decisive. For example, centralized associations are predominantly non-stock corporations; yet many federations, as the Michigan Potato Exchange, take the non-stock form. The way in which these two types of associations handle marketing problems at the central market is after all much more important than these distinctions in form of organization.

ORGANIZATION OF THE BURLEY TOBACCO GROWERS ASSN.



An analysis of the form of organization of these associations does show, however, that the program of the centralized type is fundamentally legalistic and involves tying the growers firmly to a rigid, formal

organization frequently set up according to political divisions, with all the necessary legal devices to compel members to obey all the provisions. The federation program, on the other hand, is more democratic. It proposes to accomplish the same end by leadership, education, and incentive, and leave the member more free to follow instructions or not as he sees fit. It has faith that if the central federation performs its part well, the members will be loyal to it. Its organization is therefore built on the basis of natural social and economic groupings. This is the most important difference between the two types of organization. It is a significant fact that Danish co-operatives are very similar in this respect to the federations of Minnesota and neighboring states.

These two types of organizations have developed under different conditions of production and marketing and they have obtained their **different characteristics** largely if not wholly from the different problems with which the organizations were confronted in the central market. Some of these central market problems and the way in which they are handled by overhead associations are as follows:

Control of quality.—It has been pointed out that local co-operatives, by failing to market a product of uniformly good quality, have been unable to obtain good prices for products and to develop regular outlets for them. Managers of the locals are too often ignorant of central market requirements, or indifferent to them; and when they know the kind of product wanted, they do not always have the co-operation of producers.

A central co-operative association can therefore provide market specifications for the local markets. It may enforce them and it may also help the local market to secure the co-operation of the growers to make the specifications effective. The amount of authority to enforce these specifications that should be left to the central should probably depended upon the type of commodity. Associations of the centralized type, for example, have been most successful in marketing products graded and packed locally and sold by brand. Where the improvement in quality requires the full co-operation of producers in the standardization of varieties and methods of production, as for wheat, livestock, or butter, the federated type is more effective because it has locals to maintain the contacts between the central and the producers. Local warehouse or manufacturing associations might establish these contacts. However, in centralized associations, the warehouse is usually owned by a corporation organized on a district or state basis.

Standardizing production.—This is essential to improvement in quality and to economical marketing. The federation with its superior local contacts is better organized than the centralized type, however, to enlist the support of producers in the matter of selecting pure seeds

and reducing the types or varieties produced to a few that are best adapted to conditions.

Adjusting production to consumption.—Public and private agencies disseminate a great deal of market information that is useful in helping growers to decide what to produce, but a large part of it does not reach them. A central organization may therefore render an important service in interpreting and supplementing such information and providing the means of getting it to the growers. Here again the federation offers the superior facilities for getting the information across to the growers.

Stabilizing production.—Co-operation has done very little to eliminate the great social waste that results from cycles of over-production and under-production. Local co-operation obviously can do very little with it, except perhaps in the case of local milk producers' associations and local fruit and vegetable growers' associations. Central market co-operation has also done very little with it, partly because most co-operatives have been busily engaged in handling more immediate marketing problems, and partly because they have been uncertain of the legality of control of output. The Clayton amendment specifically exempts horticultural and labor organizations from the provisions of the Sherman Anti-Trust Act. About thirty states also exempt co-operative associations from the anti-trust laws of their states. However, these laws have never been thoroly tested and it is probable that the courts will not uphold a policy of restriction of output that raises prices over any considerable period. More recently the Capper-Volstead Act exempts co-operatives from the federal anti-trust laws only providing they do not "unduly enhance" the price.

There are three possible methods of trying to handle this problem. The first method is to permit co-operatives to control production. However, such a policy would probably ultimately result in a disadvantage to the producer. Moreover, such a policy offers no protection to the public against unreasonably high prices. The second method is to try to determine "necessary price" and expect the courts to declare any price not unduly enhanced that does not call forth more than the necessary supply. The objections to this are that necessary price is very hard to determine, and that growers would not be satisfied with such a price if they got it. A third method is to let some impartial public agency determine in advance the acreage that is needed to supply the growing population, assuming normal yields, and then to permit growers' organizations to restrict acreage to that price if they wish. The public's interest is thereby protected; producers' organizations would not be engaged in a losing game of matching wits with

better organized groups; and for the present at least the collection and analysis of market information would be better done than when undertaken by the co-operatives.

Undoubtedly overhead organizations furnish the best means of disseminating the information. However, as no organization will be given authority to say how many acres a member shall grow, and as the means of control will be education and publicity, it is likely that a federation will be fully as effective in such a program, if not more effective, than a centralized type of organization.

Controlling consumption to fit production.—Advertising and publicity campaigns to increase consumption to take care of an increasing production, or of a surplus resulting from large yields, can undoubtedly be handled more efficiently by an overhead organization than by locals. In fact, except perhaps in the case of local milk-producers' associations and local fruit and vegetable associations producing for a local market, the locals are not fitted to conduct such campaigns independently. Many overhead organizations will of course discover that it will not pay. Those marketing staples, such as grain, cotton, and livestock, for example, or those marketing products that must be processed, which constitute about seventy-five per cent of the value of farm products, will probably find it not worth while. On the other hand, the experience of several organizations marketing luxuries or semi-luxuries that are ready for consumption indicates that advertising such products pays. It should be noted, however, that most of these campaigns have tested advertising chiefly during a period of rising incomes when the consumption of all luxuries was increasing.

Examples of successful advertising by both federations and centralized organizations might be given. The essential to success in such a program is a large volume of standardized products. This does not necessarily mean a large proportion (85 or 90 per cent) of the supply; nor is it necessary that the central do the enforcing of the specifications. In general, however, the centralized organizations with authority to enforce specifications are more likely to secure proper conformity to them than are the federations.

Controlling the flow to market.—The problem of determining when to sell differs as between those overhead organizations that control most of the supply and those that control only a small proportion. Under the first condition, a regularly quoted price ceases to exist. The organization is therefore forced to study the market and decide upon the price that is necessary to move the crop; or it must know the rate of consumption so that it can market at a rate that will realize the greatest possible return. Whichever method is used, the organization must have much more information than is now available. It must

know the factors affecting supply and demand, the location of stocks, and the like. Moreover, it will probably discover that the most practical procedure is to use a combination of the two methods. If a forecasted price is used, a knowledge of the rate of consumption will be needed to determine whether the forecasted price is proving to be too low or too high. Conversely, a forecasted price will be a check on the methods of feeding the market. Such a method can not of course be used without organized exchanges.

If an association had only a small proportion of the crop under control, on the other hand, there will be enough of a market organization that market prices can be quoted. All the association will need to do then is to determine the necessary price and sell when the market price reaches this level. The objection that the association can not handle the problem to the advantage of its members under these conditions is not valid, for altho the market as a whole may not be properly fed, if the particular association accurately forecasts price it will not need to sell below that price in order to dispose of its whole supply. For the same reason, an association may successfully forecast price with other co-operatives in the field, if its method of forecasting is good. For example, if competing associations sell below its forecasted price, the association needs only to wait until their supply is exhausted. The price will then be as high as the forecasted price, probably higher, as supplies are consumed relatively too fast because of the too low price during the first part of the season. Several associations, each handling a small proportion of the supply, may therefore secure results as good as one controlling most of the supply. In fact, during the experimental stage, the mistakes of several small associations would probably be less serious than the mistakes of one large association.

The problem of stabilizing prices is therefore much more difficult than most people who consider it realize. Moreover, the present method of trying to outguess the market is failing more times than it succeeds, and it probably will continue to fail. What is needed is better information regarding the factors affecting price. This calls for the development of statistical methods to determine and measure these factors. In other cases it will require the securing of more information than is now collected. This means that much statistical research work must be done before associations can make much headway with the problem. Much has already been done in forecasting the price of potatoes, however; and other products are being studied. The preparation of methods for forecasting prices and feeding the market will obviously progress much more slowly for some products than for others. But eventually a body of method and experience will be accumulated that

will enable overhead organizations to improve greatly upon their present guessing of the market.

Distributing the product.—An overhead organization can render a valuable service by directing shipments to the right market. This is especially true of those products, as potatoes, that are distributed through decentralized marketing systems. The collecting of the necessary demand information may be done by public agencies, by commercial agencies with nation-wide distributing service, or by the co-operative company itself. The directing of the shipments should be left to the central agency, particularly when perishable products are marketed. No plan of giving control to the local or the district is likely to be satisfactory. Here, then, is where centralized control of a large part of the supply seems very desirable.

Inspecting the product.—A central organization can supplement the services of dealers, when it is selling through some agency other than its own, and of public inspectors, by examining cars upon arrival and putting them into condition for sale.

Handling claims.—The handling of claims against railroads and other agencies for damage in transit, overcharges, unwarranted rejections, and the like is a problem too difficult for country shippers.

Selling.—Producer-owned selling agencies probably command greater confidence from farmers and local associations than private agencies. Whether they deserve this confidence depends entirely upon the individual agency with which the co-operative is compared. Most private agencies are efficient and trustworthy; but unfortunately there are some that can not be so described. Producers are therefore interested in having their own representatives in the central market.

Co-operators are not agreed as to how much of the channel of distribution overhead organizations should control. In practice, they generally go no further than the central wholesale market, altho there appears to be a rather prevalent idea that co-operative associations should control the product clear through to the consumer. It is pointed out in previous discussions that this idea is held in the mistaken belief that manufacturers usually completely control the marketing of their products. Some savings may be effected by such a policy. Most of those that have gone further than the jobber, commission merchant, or auction company, however, are those that are selling an advertised, branded product whose outlets they want to control in order to utilize the large investment in advertising. This, by the way, is the principal reason for integration in the manufacturers' market.

Bargaining and price policy.—Closely associated with this belief in integration is the faith of producers that overhead organizations will

realize some bargaining advantages. The individual producer and local co-operative are not in a position to realize a full competitive price for their products. Co-operation may put them on an equal basis with the buyer; it may even give them an advantage. It is very easy to exaggerate these gains, however, as in a freely competitive market the bidding of buyers against each other forces them to pay a price that gives to the seller any advantage that they have in sources of market information and the like. The gains will be larger for products marketed by private sale than for those marketed through exchanges and auctions.

Financing.—An overhead organization with adequate control of the product and proper warehousing facilities, can borrow money at the rates prevailing in the central market or even in the large financial centers. Moreover, the basis of credit may be improved by standardization of production and grading. The cotton growers' associations have made some notable showings in interest charges.

Elimination of competitive wastes.—Duplication of service and uneconomical practices are wastes of the competitive system of marketing that the local co-operatives have not eliminated. Nor have overhead organizations made much headway with the problem. Here and there, however, they have stopped the needless competition of locals.

Improvement of business practice.—No stage in the marketing process offers so many opportunities for improvement as the local market co-operatives. Poor management, uneconomical practices, and inadequate accounting systems make this probably the most inefficient link in the chain of middlemen. Public support is inadequate to carry on the necessary educational work. An overhead organization is therefore the best means of developing sound principles of business practice among locals.

Utilization of by-products.—The volume of business of local co-operatives is too small for the economical development of by-products. Only by the federation of locals or the formation of central organizations can otherwise wasted materials often be utilized.

Development of research.—A large amount of research is needed if these problems of marketing are to be properly handled. The limited resources and location of the locals make it impossible for locals to do anything with them. Public agencies can assist, but there are many problems which they can not properly handle. The overhead organizations must therefore supplement the research of public agencies. Several of the large co-operatives have already shown that they can do this very well.

It is evident from the foregoing discussion that the central market problems of co-operatives are many and complex. Success in handling

them requires careful planning and intelligent management. Moreover, the proper kind of organization depends upon the relative importance of the marketing problems to be handled. Federations can handle those problems that require the co-operation of the individual producer better than the centralized organization; whereas the centralized type that emphasizes the control of a large proportion of the supply can handle the distribution of products between markets to advantage. The type of organization is not important in handling such problems as when to sell, utilization of by-products, and bargaining. Intelligent management is the essential to success with these.

Pooling.—Pooling by central marketing organizations involves three important management problems, namely, paying for quality, prorating expense, and the pooling period. Each of them differs from similar problems of the local only in degree. The pool of an overhead organization must draw its product from a large area. Hence it usually has such a wide variation in quality that the existing grades do not give a sufficiently fine classification to provide for all recognized price differences. The result is that proper payment is not made for quality. Payment may be made on the basis of prevailing values for quality. At present, however, few pooling methods as used over wide areas pay adequately for differences in quality.

Pooling expenses likewise becomes more difficult as the market area increases. Such questions arose as the division of expenses between localities and growers. For example, shall losses in transit be charged to all growers or only to the locality from which the product is shipped? Charging the proper expense to different kinds of shipments also becomes more difficult.

The pooling period is not important for products that are produced all at one season. However, if production is continuous, and costs and prices are seasonal, it becomes important to select a pooling period that makes it possible for the farmers to be paid on the basis of the price that prevails at the season of the year for which he has planned the producing and marketing of his product. The question of storing complicates the pooling problem.

The local.—A local association is a desirable feature of an overhead organization. It establishes between the central organization and the individual producer the contact needed for carrying on educational and publicity work, while at the same time the producer's active participation in the management of the local commands his sympathy for and loyalty to the policies of the central. Moreover, in case the central fails, the locals still provide a market, and the foundation for the building of a new central organization.

The status of the local in any marketing system should depend upon the nature of its marketing problems. The tendency among federations is to curtail the authority of the local in the matter of sorting, grading, and packing, and controlling distribution. Centralized organizations, on the other hand, are organizing locals. Future organizations will therefore doubtless represent various degrees between the extreme federated type and the centralized type, each adapted to the problems of the specific product marketed.

CONCLUSION

In its very inception, this bulletin has placed much more emphasis upon form of organization than it deserves. The whole drift of thought at present is in that direction. One might conclude from discussions of co-operative marketing that all that is necessary in order to attain success is to organize according to the right plan, that all our efforts at co-operation in the past have been more or less futile because our plan has been wrong. Accepting this philosophy, we put on a membership campaign, expecting to work out marketing methods later—satisfied that if only we can get enough of the crop signed up, we can not fail with our marketing—and expecting growers to take it upon faith that we shall be able subsequently to work out successful marketing methods. The over-emphasis previously noted upon membership contracts, liquidated damages, and the like, is but an instance of this.

As a matter of fact, the most enthusiastic and successful membership campaign that was ever made might easily be followed by failure because of a poor system of grades, a poor pooling plan, or a foolhardy attempt to outguess the market. Such things have happened, and will happen again and again in the future. The real problems of co-operative marketing are the problems of control of quality, pooling, forecasting necessary price, and feeding the market, financing, distribution, and the like. It is upon our success in solving these that success in central marketing will largely depend. Unfortunately it takes time to solve such problems. But our co-operative marketing enthusiasts do not wait. To organize is the thing, seems to be their dictum—the question of marketing methods will be handled when it arises! For their over-confidence in this matter, many will pay the price of failure.

The problems of control of quality, pooling, feeding the market, and others must be worked out for each product. There is no one method of pooling that will fit all commodities; neither will it always be possible to reason out in advance what pooling plan will work best for any commodity or any one district—what the period should be, what the

area unit should be, what grade pools there should be, and how pooling and storage shall be arranged. The same is true for all marketing problems.

As one examines the history and records of co-operative central marketing organizations in this country and abroad, one conclusion stands out clearly from the start, namely, that there is no magic formula that insures success on every occasion. Developing successful co-operative marketing methods in the central market is a slow, hard process, as it has been in the local market. We hear much of the marvelous success of co-operative marketing in Denmark; yet the Danish farmers feel that they are about as far from having solved their marketing problems as are the farmers of Minnesota. The same is conspicuously true of California farmers. Great progress has already been made in Denmark, in the United States, and in other parts of the world; but the task is only well begun.

The importance of the foregoing statement can not be exaggerated. Many promoters of marketing organizations have a way of presenting their proposal as the last word in perfection, as if practically certain of success, and almost guaranteed to save farmers from whatever economic plight they may find themselves in at the time. In the almost inevitable reaction that follows, the whole cause of co-operative marketing suffers severely. It would have been much better if their proposals had been fairly presented in the first place, with a full and free discussion of all the problems and difficulties likely to appear, and a fair statement of the extent to which the then prevailing predicament of the farmers was due to faulty marketing; and a conservative estimate of the gains likely to result from the proposed organization.

Perhaps it is appropriate to ask at this point what gains reasonably can be expected from a central marketing organization. No one really has any basis for predicting the amount of such gains. But if promoters are going to make heroic guesses on the subject, students of co-operation owe it to the public to do the same. Hence the gains will vary greatly as between commodities because of differences in the degree of organization of the present market for them. As a sort of rough average of all commodities, the authors believe that the *potential* gains on Minnesota products from several of the most important improvements in our marketing system, or in production as it relates to marketing, rank in importance about as follows:

1. By stabilizing production—adjusting it to changes in demand and to changes in the business cycle, and eliminating cycles of production.

2. By improving the organization and management of the locals or in other ways performing the local market functions more efficiently.

3. By improving the quality of production by standardization of varieties, better selection and treatment of seed, better care of the crop, better harvesting methods, etc.

4. By controlling the time of movement to market.

5. By better sorting and grading.

6. By better distribution between markets.

7. By advertising, especially advertising an extra large crop, and by developing new markets.

8. By securing equality or better in the matter of bargaining, and taking away from buyers any possible monopoly advantage they now enjoy.

Obviously, the ranking of these eight points for butter is much different from the ranking for wheat or corn or livestock or potatoes. Also the ranking for Kentucky or Texas or California would be different from that for Minnesota.

Also, the foregoing ranking is on the basis of potential gains, not probable gains. Altho potential gains from stabilizing production are great, the probable gains from this source are not very great in the next few years—this is a problem for generations, even centuries. As to gains *reasonably possible* in the next ten years, the ranking would be more as in the second column of Table IV. As to gains *probable* in the next ten years, the ranking will be more as in the third column of this table. The reason that No. 4 is put so far down in the last list is that in the next ten years, in view of our present understanding of the problem, the mistakes that will be made may entirely offset the gains.

TABLE IV
ESTIMATED RANKING OF SOURCES OF GAIN FROM CENTRAL MARKETING CO-OPERATION
IN MINNESOTA

Sources of gain	Potential gain	Possible gains in next ten years	Probable gains in next ten years
Stabilizing production	1	7	8
Improving the locals	2	1	4
Improving quality produced	3	4	3
Controlling flow to market	4	2	6
Better sorting and grading	5	3	1
Better distribution of product	6	5	2
Advertising and developing markets	7	6	5
Price control (monopoly and bargaining).....	8	8	7

The probable gain to producers and consumers in the next ten years from these eight sources will probably range for the various Minnesota products from less than 2 per cent to more than 10 per cent,

with an average of less than 5 per cent. It must be remembered that livestock, grain, and dairy products constitute the bulk of Minnesota's production, and upon these commodities the gains will be relatively small. Of this 5 per cent or less of gain thus so boldly predicted, the producers will receive the larger part, especially if other states and other countries fail to make equal improvement in their marketing of the same products.

In the end marketing will be efficient in proportion to the intelligence, skill, and understanding of those who are responsible for it. One of the weaknesses of co-operative marketing of farm products is that responsibility for it rests in the last analysis upon the farmer, and farmers suffer severely from a vast amount of misinformation on matters relating to marketing and prices. Milk producers' associations, for example, suffered a great deal at the start and still suffer at times because of mistaken notions of their members as to the relation between price and cost of production. A state wheat growers' association even as late at 1922-23 decided to hold its wheat for a higher price partly because the management believed that the price of wheat could not possibly stay so far below the cost of production for more than another month or two. Surely it is highly necessary that those who are presenting plans for better marketing shall on all occasions use only right information, correct analysis, and sound arguments. Better frequently that a particular organization wait a few years before getting under way, than that it be sold to the people on the basis of a whirlwind campaign of misinformation and exaggeration. It may take a generation or two to root out the evil that is thus planted, and all the while it is bearing bitter fruit.

In this connection, it can not be too strongly urged that the proper basis upon which to put over a campaign for membership is not one of developing or appealing to class hatred. The Capper-Volstead Act and the Minnesota co-operative acts are not "vicious class legislation," as is sometimes stated even by their defenders. They are legislation in the public interest, never would have been passed on any other basis, and would not stand the test of the courts on any other basis. An old-fashioned concept of class legislation made it include any legislation designating a special class for special treatment. The criterion at present is whether it benefits or injures one class. As J. D. Miller, of the Dairyman's League, so well states: "The law is not so poor a thing that it prevents the state from authorizing combinations that will promote the public good at the same time that it prohibits combinations detrimental to the public good."³⁰ The co-operative marketing program should be presented to the growers on the basis that it will inure to the common good as well as to themselves. It should be presented

to the general public as well as to the growers; and it should be presented to the public fearlessly on the basis here outlined.

For the same reasons it is bad policy to go before the business men of the territory which is being organized and tell them that they must support the campaign because their prosperity depends upon the prosperity of the farmers. They should be told instead that this is a program dedicated to the common good, that Congress and the state legislature have authorized such programs and furnished the legal basis for them, in the faith that they will redound to the common good, and that altho it will help make the growers in their territory more prosperous, it will also make the nation more prosperous, and all its citizens, including their fellow townspeople, except the very few who may lose their business altogether.

Even more important is it that campaigns be conducted in a spirit of broad-minded tolerance. Growers will be found everywhere who object to five-year contracts. The pressure which has been brought upon them to sign has occasionally been so strong as clearly to amount to intimidation. The never-failing result of such tactics has been a growing feeling of ill-will in the community, preparing the way for bitter factionalism. Even within the last year, fields and buildings have been destroyed in such conflict. This, surely, is not the way out.

The foregoing is offered as an interpretation, in terms of Minnesota's conditions, of co-operative central or overhead marketing organization as at present developed. The subject is one which is rapidly developing in both economic and legal aspects. A few years hence, some of the tentative conclusions above presented may need to be modified. The authors will be ready to make these modifications whenever they seem called for by new facts and new experience. It is not likely, however, that the principles upon which the conclusions of this bulletin are based will be modified very greatly in the near future.

⁸⁰ 7 Cornell Law Quarterly, pp. 293-308.